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BEFORE THE U.S. HOUSE OF REPRESENTATIVES
COMMITTEE ON AGRICULTURE
SUBCOMMITTEE ON GENERAL FARM COMMODITIES
AND RISK MANAGEMENT

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Mr. Chairman and members of the Committee, thank you for the invitation to participate in today's hearing. I appreciate the opportunity to discuss developments of the Board of Directors (Board) of the Federal Crop Insurance Corporation (FCIC) since last year's oversight hearing. This morning, I will briefly review some of the Board's major activities, including approval of new products and pilot programs, changes in existing products and key issues addressed by the Board.

Mr. Chairman, the Federal crop insurance program is growing and improving and serving the public well. In just the past five years, the number of acres insured through the program grew by 14.7 million, as more farmers saw the value of the crop insurance safety net and as more products were developed and approved for more crops in more locations. The program now offers 22 insurance plans on over 350 agricultural commodities in all 50 states plus Puerto Rico. The FCIC Board has focused this past year in evaluating the product portfolio, considering new products offered to the program and expanding existing products into additional states.

The Board has benefited greatly from the experience and broad knowledge of its members. They have been, and are, persons of accomplishment in the worlds of agriculture, insurance, agribusiness and other areas. This past year saw a change in the Board as three members left the Board due to expiring terms or other reasons, and three new members joined the Board. We thank those leaving for their excellent public service: Susan Fitzsimmons, Roger Swartz, and Christopher Watt. New members include: William (Bill) Classen, who fulfills the requirement for a member with experience in the crop insurance business; Luis Monterde, a specialty crop producer from Mississippi; and Mike Pickens, experienced in regulation of insurance. Other members include: John Askew, a producer from Iowa; Frank Jones, a producer from Texas; Tim Kelleher, a producer from California; Ross Davison, administrator of the Risk Management Agency (RMA); JB Penn, Under Secretary for Farm and Foreign Agricultural Services, and myself.

The Board is charged with general management of FCIC and takes that responsibility very seriously. We could not succeed without very close interaction with the employees of RMA and the Office of the General Counsel, who work tirelessly to provide us the information and analysis we need for our deliberations, and we thank them for these continuing efforts.

Actions on New Products, Improved Products

This past year, the Board has taken significant actions affecting the Federal crop insurance program. We have received proposals for many new products, directed expert reviews for the appropriate offerings, approved new products, approved modified pilot programs with improvements, and terminated some products that were not serving the needs of producers. I will review a few of these actions which have had a positive impact on the crop insurance program as a whole.

Two actions taken by the Board this year involved resolving issues of concern related to outstanding livestock products. The Livestock Risk Protection (LRP) pilot plan of insurance for fed and feeder cattle and the Livestock Gross Margin (LGM) pilot policy for hogs were approved by the Board under Section 508(h) of the Federal Crop Insurance Act (Act) which authorized the submission of private policies. In early 2004, the Board withdrew these livestock products, pending review and modification, following cessation of sales of LRP cattle as a result of the discovery of a BSE infected cow in Washington State in December 2003 and due to other issues related to LGM. RMA successfully worked with the owners of both of these products to identify modifications requested by the Board, making it possible for the Board to re-open sales of the improved plans of insurance beginning September 30, 2004. The modifications made to the livestock insurance plans included procedures for the suspension of sales of the product in cases of catastrophic events or highly volatile futures market prices and other procedures to minimize adverse selection by insureds.

The Board remains concerned over the marketability and the appropriateness of these products as a long-term offering of FCIC. Consequently, the Board has required a thorough evaluation of the performance of the livestock pilots after one year of operation is completed on September 30, 2005.

During the past year, the Board also approved the significant expansion of a relatively new product, Adjusted Gross Income-Lite (AGR-Lite). AGR-Lite was developed by the Pennsylvania Department of Agriculture and first offered in 2003 in Pennsylvania. In the two years following its introduction, AGR-Lite was expanded to 16 states (including Pennsylvania), and for 2006 will be available in a total of 18 states. There appear to be additional states currently working with Pennsylvania to request that AGR-Lite be expanded into their states.

AGR-Lite covers the adjusted gross revenue from the whole farm based on five years of Federal tax return data and expected farm income for the current year. It is a simplified version of the Adjusted Gross Revenue (AGR) pilot plan of insurance and uses the AGR Handbook and rating methodology. AGR-Lite can potentially fill an important void in FCIC's product line by appealing to small-to-medium size producers of livestock and specialty crops. AGR-Lite, as a new plan of insurance, has had limited participation and continues to undergo revisions for improvement. In 2004, there were 96 policies sold, and for 2005, there are 148 policies earning premium with an average of three agricultural commodities covered per policy. Those sales compare to an average of 444 traditional MPCI policies for one agricultural commodity.

AGR-Lite has a $250,000 liability limit and that is most likely one reason for the somewhat limited participation, including participation by producers with livestock. The liability limitation exists as an eligibility requirement because of the relationship between the cyclical nature of livestock prices and the AGR/AGR-Lite rating method. RMA currently has a contractor working to determine the most effective and actuarially sound methods to use in rating various types of livestock under the AGR plan of insurance. Other reasons the participation level is low may be related to the learning curve of a financial product as compared to a production agriculture type of insurance product, as well as the cost of delivery. On April 28, 2005, the Board sent for expert review a series of potential modifications of AGR-Lite designed to improve the product and increase participation.

Answers to some of the questions surrounding the limited participation may also be forthcoming soon, as RMA entered into a contract for a formal evaluation of the AGR pilot program last summer. This in-depth evaluation will review all aspects of the AGR pilot program including a review of program, listening sessions with both producers and approved insurance providers, underwriting, actuarial analysis, tax issues, and reinsurance. The evaluation is scheduled to be completed in early December 2005 after which the Board will place AGR under consideration for continuation, continuation with modifications, or termination.

At our most recent Board meeting, held last week on April 28, the Pennsylvania Department of Agriculture presented proposed revisions for the AGR-Lite program. The Board acted to send the proposed revisions for expert review. We continue to believe that the growing pains of this program can be overcome with time and diligence, and that it will prove to be a very useful product for small-to-medium size, diversified farmers and ranchers.

The Board continues to look for ways to improve the risk management capacity of farmers and ranchers. In May 2004, the Board, responding to the needs and requests of producers, authorized the implementation of a Silage Sorghum Pilot plan of insurance for 2 counties in Colorado and 37 counties in Kansas. The maximum coverage level for this pilot program is limited to 75 percent and the price election is limited to 80 percent of the price election for corn silage. Sorghum varieties grown for harvest as silage are eligible for coverage under the new program beginning with the 2005 crop year, with the pilot continuing through the 2008 crop year. Non-silage varieties of grain sorghum are not covered under this pilot program.

In addition, growers of grain sorghum felt that they had fewer risk management options than did corn and soybean growers. In October 2004, the Board approved the Group Risk Income Protection (GRIP) plan of insurance for grain sorghum, beginning with the 2005 crop year, for all states and counties currently approved for the Group Risk Plan (GRP) giving grain sorghum growers an additional insurance choice. GRIP was initially submitted and approved under Section 508(h) but it is now owned and maintained by RMA. Since GRIP for grain sorghum will only be offered in areas where GRP is offered, sufficient actuarial information was available for this implementation.

Dealing with Existing Pilot Programs

In addition to approving new crop insurance programs, improving the existing portfolio of products remains a high priority for the Board. As part of a broad portfolio review conducted last year, the Board contracted for the development of an analytical tool to help measure the performance of existing products and identify changes that would improve their usefulness. That analysis tool, which encompasses over 70 questions, is now being integrated into the business processes of RMA. It will be used by RMA to assess existing policies and can be used by new product developers and contracted evaluators.

The Board has responsibility for eliminating those programs that have not proven to be in the interests of producers or cannot be demonstrated to be actuarially sound. In 2004, the pilot program for crambe was terminated by the Board and the Pilot Coverage Enhancement Option, or CEO, was terminated following the 2005 crop year in most states.

Pilot programs for mustard, mint, wild rice, and cabbage were evaluated by the Board and the Board determined them to be successful and voted to convert them to permanent programs. This vote culminates years of extensive scrutiny that the programs went through to achieve final approval.

The value of pilot programs was demonstrated through two significant actions this past year. The Board terminated the existing Pilot Group Risk Plan Rangeland Program and replaced it with a new Pilot Group Risk Plan Rangeland Program, which has a more accurate index for the 2005 and succeeding crop years. Similarly, the Board dealt with the Sweet Potato Pilot program this year. This pilot program, introduced in 1998 for Alabama, Louisiana, and South Carolina, had high loss ratios and program integrity vulnerabilities. The Board asked RMA to perform a comprehensive review of the program and upon its review of the findings, decided to continue the existing Sweet Potato Pilot Program for the 2004 crop year, subject to changes to ameliorate the worst problems, while a new Sweet Potato Pilot Program was developed for the 2005 year. After contracted experts reviewed the new proposed program, the Board cancelled the previous flawed program and approved the new one in October 2004.

Improving Board Processes

The Board regularly reviews its processes through its Governance Committee and through the Board as a whole. This past year, the Board determined that it was necessary to clarify its expectations, and the standards it uses, with respect to marketability of new products and reimbursement of research and development and maintenance costs in order to improve decision making regarding the approval of private products submitted under Section 508(h) and 7 C.F.R. part 400, subpart V. The Board must determine that the interests of producers are protected before it can approve a submission by RMA or a private entity and, thus, the marketability of a submission should be considered when determining whether the interests of producers are protected. Therefore, the Board has requested applicants to submit additional information to substantiate the marketability of their submission. Such information includes focus group results, market research studies, qualitative market estimates, effects upon the delivery system or ancillary participants, correspondence from producers expressing the need for such product or plan, responses from a reasonable representative cross-section of producers to be affected by the product or plan, and correspondence from approved insurance providers and reinsurers expressing willingness to sell and support such a plan. If the producer does not see it as attractive and the approved insurance provider is not in favor, the wisdom of approving a new submission would be in question.

The Board also now asks that a submitter fully disclose and document requests for reimbursement of contracted expenses and professional fees associated with a submission. We find that certain information is sometimes ambiguous or fails to fully articulate business relationships, and that such information is needed in order to determine the reasonableness of these expenses. To remedy this situation, the Board now asks applicants to include the relationship, if any, between the applicant and any contractor or professional, such as parent company, subsidiary, etc. Further, the Board examines contracted expenses and professional fees broken out by line item to include individual names, rate of pay, hours allocated to the submission, benefit rate and overhead for the professionals and all persons who make up the contracted party who had substantive involvement in the development of the product for which reimbursement was sought.

In evaluating whether the interests of producers are protected, the Board also believes that due to the finite nature of resources available to FCIC, the level of expected future maintenance costs must also be considered, including costs associated with changes to automated systems, and the impact to the delivery system to assure the ability to adequately and appropriately inform, service and timely meet all obligations for eligible producers. Therefore, the Board now asks applicants to provide a comprehensive estimate of future maintenance costs for each of the next four years for the submission and the basis for which such maintenance costs will be incurred, including, but not limited to, any anticipated expansion, the generation of rates, the determination of prices, automated systems impact, delivery costs, contracted costs and any other costs that the applicant anticipates will be requested for reimbursement.

PRP—a Major Issue

A major issue that the Board addressed during the past year and an interest expressed for this hearing is Section 508(e)(3) of the Act, which provides for the possibility of a premium reduction for producers. The issue of a Premium Reduction Plan (PRP) has led to considerable debate, divergent opinions, and much deliberation by the Board. Issues regarding the legality and equity of such a plan have arisen. To address all the issues, in November 2004, the Board directed the FCIC to proceed with the notice and comment rulemaking process in this matter as expeditiously as possible. Let me briefly provide the context in which the issue arose for the Board.

Section 508(e)(3) requires the FCIC to allow approved insurance providers to offer a premium reduction plan if they meet the requirements of the law. In 2002, one company, Crop 1, requested Board approval to offer a PRP. By Board resolution in December 2002, the Board established certain standards that such a PRP should meet. The Board also directed RMA to develop more detailed procedures by which that particular company could operate a PRP and by which others could also apply to operate such plans. Since then, several other approved insurance providers, representing over 80 percent of the crop insurance business have requested approval to offer a PRP of their own particular design, including substantial variations from the single plan approved in accordance with Board-established procedures. However, those plans have presented significant implementation and regulatory issues for RMA that were not contemplated by the existing procedures. The Board decided that all stakeholders, including the producers who stand to benefit from such plans, should have an opportunity to present their views. Accordingly, RMA is proceeding with notice and comment rulemaking to establish a comprehensive framework by which such plans will be evaluated, approved, regulated and operated. The comment period for the proposed rule ended on April 25, 2005. RMA will consider all comments received so that the final rule will allow them to administer Section 508(e)(3) of the Act equitably and to the benefit of all producers, large and small, while maintaining the integrity of the Federal crop insurance program.

During this rulemaking process, the Board has provided its counsel to RMA on a range of PRP-related issues. The Board created an ad hoc committee that reviewed the proposed rule and will continue to serve as a sounding board for RMA during the development of the final rule.

After the rule is issued, the Board will review with the manager of FCIC all submission for approval of a PRP.

The Board is fulfilling and will continue to fulfill, its statutory responsibilities, including the provision of oversight, guidance and direction to FCIC and RMA. At each meeting, the Board reviews different aspects for RMA's activities in the discharge of the Board's general management responsibilities. Each Board member is pleased to have the opportunity to serve and we all work diligently to ensure the effectiveness and efficiency of the nation's crop insurance program.

That completes my remarks.